The Canada - USA Trade Agreement and the Yukon

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Yukon
Economic Development:
Mines and Small Business

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INTRODUCTION

The proposed Canada-U.S. Trade Agreement alters a number of the trade tools that currently shape the economy and trading patterns of our two countries. This change is inevitable, as economies have always been affected by trade relationships. However, as with any agreement, we need to examine the Canada-U.S. trade agreement as Yukoners. What does the Trade Agreement do for the Yukon?

New national initiatives affect the Yukon in different ways than the rest of Canada. Tax Reform, for example, will alter the flow through tax credit incentives significantly. Less incentive to invest in mining exploration will likely affect the Yukon more than any other region. Revisions to the Canadian Constitution will make the Yukon more of a colony with less control over its own future. The Trade Agreement will also affect the Yukon in different ways than the rest of Canada.

In 1985, The Royal Commission on the Economic Union and Development Prospects for Canada (the MacDonald Commission) recommended that the Government of Canada begin negotiations with the United States to reach an agreement on a substantial reduction of tariff and non-tariff barriers. The Commission also recommended that special consideration would have to recognize the distinctive interests of northerners.

The Yukon Government has been a participant in some of the consultations related to the Canada/U.S. trade agreement. Officials have consulted with industry through the Yukon Economic Council and made presentations on behalf of the Yukon. While government officials were briefed at various trade negotiation talks, our government was excluded from the First Ministers discussions on the Trade Agreement.

To better understand how a trade agreement might affect the Yukon, the government contracted a study in early 1986. Because negotiations were just beginning when the report, "The Impacts of Canada/U.S. Free Trade on the Yukon Economy" was commenced, assumptions about the possible terms of an Agreement had to be made. Unfortunately, these assumptions are very different than the final Agreement that was negotiated. Consequently, the 1986 study provides little assistance in determining the impact of the Trade Agreement.

The Canada/U.S. Free Trade agreement does not create a true free trade environment as assumed in the previous study, it merely changes a number of the trade rules and regulations affecting trade. The Trade Agreement:

- eliminates the tariffs on a number of goods and services traded;

- revises the method for handling trade disputes between the two countries;

- changes foreign investment restrictions;

- creates a single north American energy market; and,

- alters the way regional (northern) development policy is shaped.

In reviewing the breadth of this agreement, one must realistically consider how it will affect our plans for the future. As a part of the Yukon's ongoing examination of the trade agreement, this document has been prepared to discuss the different aspects of the agreement and how it will affect the Yukon.

YUKON'S COMPETITIVE TRADING POSITION

The Yukon and Canadian economies have some significant differences as trading regions. The Canadian economy has been growing and diversifying while the Yukon economy has been going through major booms and busts. Canada is a net exporter, exporting more goods than importing. The Yukon is a net importer, we import more than we export. The Yukon imports $200-300 million per year more in goods and services than we export.

When discussing the benefits of trade, what's good for a net exporter is not necessarily good for a net importer. The jobs, businesses and industries and benefits gained in the exporting region may be at the expense of an importing region.

The Yukon needs to diversify its economy, and develop other industries which will provide jobs and export income for Yukoners. The Yukon's main industries, mining and tourism, have had very few trade restrictions. Historically, other regions have diversified into manufacturing and processing by supporting industries through trade initiatives. These industries would not have flourished if support programs had not been available during their growth period. Where there is potential for manufacturing or processing it will need the same type of encouragement that industry has received elsewhere in Canada.

The Yukon was, until recently, one of the few regions without significant programs to support local firms. Other Canadian jurisdictions have been stimulating local industry for years to help them get established and start exporting. Countries and regions have used various trade tactics to decrease the number of imports and increase exports. This helps the country diversify and develop its export markets.

A number of trade "tools" have traditionally been used in all regions to help develop an export industry. The new Trade Agreement will alter the tools that the Yukon has to develop a broader industrial base. The following section examines how these tools have been changed.

ELEMENTS OF THE AGREEMENT

The Trade Agreement is made up of a series of elements which influence the way goods and services can be traded. These elements are listed and discussed below:

Tariffs

Tariffs are to be eliminated on most goods and services effective January 01, 1989 or, in annual increments for five or ten years. The change in tariff structure could have differing effect, depending on the competitiveness of a particular product. A number of Yukon imports and exports will be affected:

- Tariffs, as a rule of thumb, have been higher the more finished a good or product is. The elimination of tariffs will have more affect on manufactured products than raw products.

- All industries will be brought into a more open economic environment with broader markets but also fewer support mechanisms such as tariffs, and increased competition from firms in other areas who can benefit from appropriate economies of scale.

- Tariffs have been used to protect many Canadian industries. As other Canadian regions have used trade protection to help their economy grow, such as the Autopact in southern Ontario, the Yukon will lose this opportunity. The Yukon will have less tariff protection for local industry desiring to process our products.

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SAMPLE LIST OF TARIFF REDUCTION

Tariffs will be reduced over a ten year period:

One year list:	Fur/fur products
January 01, 1989	Leather
	Whiskey
	Yeast
	Animal Feeds
	Computers
Five Year list:	Some machinery
Annual Steps	Smoked fish
to January 01, 1993	All chemicals & explosives
	Furniture
	Paper& paper products
	Gold Jewelry
	Telecommunications equipment
	Hardwood, plywood, press board
10 year list:	Most agricultural products
Annual Steps	Steel
to January 01, 1998	Textiles& clothes
	Finished manufactured products
	Parkas
	Appliances

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Investment

Both countries have agreed to provide investors with national (equal) treatment for the purchase and/or establishment of business. Investment Canada will change the way it reviews U.S. investments in Canada:

- Only projects with assets over $150 million will be reviewed by Canada. As there are no Yukon firms with assets over $150 million there will be no review process for U.S. investments.

- No requirements may be imposed regarding local content and local hire specifically on U.S. investments.

Regional Development

Considering the state of regional development in the Yukon, the Trade Agreement is only one-half of a deal.
While the Trade Agreement deals with issues of national concern, it does not address regional development interests. A number of regional development tools are being altered which will affect how the Yukon can have control over its' own future:

- Regional development assistance programs will be scrutinized in the negotiation of a Subsidies Code. This code is to be developed over the next seven years. Until this code is finalized, U.S. interests will continue to claim subsidies as a basis for countervail (retaliatory) actions. The Curragh agreement with the Yukon government is an example of a regional development initiative that could be cited by the United States as an unfair subsidy.

- Local benefit programs attached to large projects which have received government assistance will be in jeopardy. Currently, the government can stipulate that, as a condition of government assistance, the company would agree to certain local hire and purchase programs. This way, a number of Yukon companies have benefited from large projects like Beaufort exploration and Curragh.

- Economic development incentive programs, such as low interest start up loans for business may be attacked by the U.S. as unfair subsidies, and the Trade Agreement offers no clarification of what constitutes a subsidy.

- Government procurement (local purchase) is an effective way of supporting local business. However, the Trade Agreement will be limiting the extent of selective government purchasing. This is important to the Yukon because the Federal government purchased approximately $4.77 million through goods and service contracts in the 1986/7 year to supply their Yukon operations. The federal and Yukon government's recently signed an agreement to increase the amount of federal purchasing in the Yukon. These type of agreements may jeopardized by the trade deal.

- Both countries have agreed to eliminate buy-national restrictions on federal procurement of goods over a threshold of U.S. $25,000 ($39,000 Cdn).

- While the deal does not bind the Yukon or provinces, there is a clause that commits both countries to further negotiations within one year, to improve and expand coverage. Yukon initiatives to buy locally like the Business Incentives Policy will under be increased

pressure to be changed as part of those future negotiations.

- The Canadian procurement market open to U.S. companies by this agreement increases by 75%, whereas the U.S. procurement market open to Canadian companies increases by only 19%. Canada's access to U.S. procurement has only marginally increased to a market of $22.6 billion up from $19 billion out of a potential $570 billion market. There are many forms of procurement protection remaining in the U.S. such as the Small-Business Set-Asides Program.

- Local tendering also helps companies to bid and win government contracts. This practice may be considered discriminatory.

A Bi-lateral Dispute Mechanism.

Trade disputes have traditionally been settled through the courts and laws of each country. The new dispute mechanism will review the application of each others laws with a bi-lateral panel. There is no major change over the previous method of settling disputes, and no guarantees that Canada will have a better hearing than before.

- The weakness of this mechanism is its dependance on decisions which are made in accordance with laws that exist at the time of the dispute. There is no security against new protectionist legislation like the U.S. Omnibus Trade Act. For example, if American lead and zinc producers felt that we had unfairly subsidized the Curragh mine, the dispute would be filed with a Bi-national Panel which would rule on the application of existing trade laws. If U.S. interests brought

forward political pressure to their government, new legislation to hinder lead and zinc exports could also be developed and applied.

- The Trade Agreement does not achieve one of Canada's main objectives in the negotiations was to provide greater certainty of access to American markets. The dispute mechanism offers no greater assurances to Canadian producers that American trade laws will not be applied against them.

Standards

Steps to harmonize standards and regulations at the Federal level will ease packaging requirements. Provinces and states will be encouraged to participate, and while compliance is not necessary, this will likely prove to be beneficial in the long run. There could be some adjustment problems as some producers have to adjust to new requirements.

Customs

The current complex regulations will be eased somewhat, with some practices being relaxed, such as paying a fee to have ones' goods processed through customs or posting a bond to ensure proper procedures are met. There will continue to be customs rules for firms to contend with, so small firms that expect an open border may still find the paperwork too onerous to successfully compete in Alaska.

Alaska state procedures such as the high bonding requirements for Alaska exports of unprocessed fish into the Yukon will still remain in effect. Only U.S. federal procedures change. Yukon business will still have to deal with the Alaskan laws.

REVIEW BY INDUSTRY SECTOR

Yukon industries are affected by the articles of the trade agreement in different ways. The following section provides some details on the affects of the agreement on industry sectors.

RESOURCE INDUSTRIES:

The trade agreement alters the way regions can manage their resources in cooperation with private interests. The ability to utilize resources for regional benefit will be severely limited. For example, Alberta has given low priced natural gas to its own petrochemical industry to help this sector grow. B.C. required mining companies interested in developing coal deposits to enter into development agreements which contained provisions for purchasing a certain amount of supplies locally. Under the new agreement, such differential pricing or procurement practices will be constrained.

Mining

There will be minor benefits for the Yukon mining industry as a result of the trade Agreement. Most of the Yukon mines have markets outside of the U.S. and, there are very few U.S. conditions on the import of minerals.

- The sale of Yukon's main metals will likely not be affected as there currently is little or no tariff on raw mineral products.

- There will be little savings on mining equipment. Tariffs have been against the import of equipment which competes with equipment produced in Canada. Since little mining equipment is produced in Canada, very little affect is anticipated.

- Chemicals and grinding steel used in processing have a tariff which will be removed, lessening the processing cost of minerals.

- The viability of mining properties will continue determined by their competitive position of northern vs. southern Canadian properties.

Agriculture

The Yukon currently produces limited quantities of vegetables, hay, grains, beef, poultry and, pork. Agriculture in the Yukon is still at a developmental stage:

- A very limited amount of Yukon agriculture is currently exported to Alaska. Little gain for Yukon producers into Alaska is likely since Alaska agriculture is subsidized.

- Cheaper food products will be available from the U.S. lower 48 states and will likely make it to Whitehorse via Seattle through Skagway. Farmers should expect increased competition from the U.S.

Fishing

Fish and fish products have few tariffs which affect their trade. Little should change as a result of the Agreement.

- With the Yukon producing more than it consumes, there should be little concern about import erosion from the U.S.

- If there are increased imports by Yukon firms from Alaska it may aggravate the current tension of overfishing in Alaska.

Fur

An elimination of tariffs will have little affect on the fur industry.

- The Yukon exports mostly raw furs which are are currently freely traded and, processed furs have a 5.8% tariff.

- Yukon Native Products has limited production of related fur products which will benefit from the tariff reductions on exports. The Agreement may provide some incentive to produce more fur products for export to Alaska.

Forestry

While the Agreement changes the tariffs on some lumber products, it does not change the 1986 Softwood Memorandum of Understanding (MOU). This MOU is responsible for a U.S. import tax against softwood lumber from some regions of Canada.

- It is unlikely that the agreement will change competitive position of Yukon firms since their main

competition (even in the Alaskan market) is with southern Canadian firms.

- The Agreement could, however, threaten other export sales (e.g. Asia and Europe) if the deal is not to be consistent with GATT (The General Agreement on Tariffs and Trade) which is the trade Agreement between 95 countries including Canada and the U.S.

Energy

The Trade Agreement creates a single, north American, energy market which guarantees access to the supply and development of energy resources to and from both countries.

- While Canada gives the U.S. open market access to energy reserves, the U.S. limits Canada's supply of Alaskan oil (the biggest supplier of U.S. oil). Canadian Beaufort oil has no restrictions while Alaskan oil does.

- There may be increased interest in the Beaufort (especially with the elimination of investment restrictions), as American firms can develop oil reserves for U.S. markets.

- The agreement also gives U.S. access to Canada's vast hydroelectric resources. In the future it could be contemplated that Yukon's hydroelectric resources could be tapped. However, the Yukon will not be able to export energy at a higher price to the Americans than to Yukoners. In the past, Quebec, Ontario, Manitoba and B.C. have exported energy at a higher cost than that which was sold to local industry. This was a way or tool for development of their economies. Today, these

provinces with huge U.S. markets are looking for secure access to the that market so they have agreed to a single pricing scheme. The Yukon's circumstances are very different

- The Agreement precludes the use of benefit programs with energy projects. Local purchasing requirements specific to U.S. oil developments in Canada would not be put in place.

MANUFACTURING AND PROCESSING INDUSTRY:

Manufacturing and processing industries have traditionally had the highest levels of trade protection. High tariff levels and business incentives have been the main tools to aid manufacturing and processing. The trade agreement takes away many of these tools, especially tariff protection.

Furniture Manufacturing

The five year tariff elimination on furniture will likely have more effect on lower priced, mass produced furniture than quality furniture. Most furniture tariffs currently average 15% depending on the product. The Yukon Based Furniture Manufacturing study stressed that only high quality furniture could be competitively produced in the Yukon.

Clothing

Yukon Native Products and other clothiers will have a lower cost product to sell into Alaska with the elimination on tariffs on clothing.

Liquors

Wines and distilled products have to be given national treatment, which means cheaper U.S. wines and alcohols for Yukoners. The requirement is that only transportation and handling costs can be added to U.S. products. Beer is exempt from the agreement. While this may appear to be an opportunity for consumers to benefit, it must be recognized that the current price differential reflects a large tax on liquor in Canada, and that is unlikely to change.

General Manufacturing

One of the Yukon's fastest growing sectors is the manufacturing and processing industry. Truss plants, a fiberglass tank facility, windows, chocolates and sausages are some examples of this growing sector. Yukon's ability to support the development of these industries and achieve the goal of a diversified economy may be restricted under the new Agreement. The gains we have made in this sector may be jeopardized if the removal of tariffs occurs before these new firms have an opportunity to establish a foothold.

SERVICE INDUSTRY:

The trade agreement fine tunes the way that services are traded between Canada and the United States.

Professional Services

Accountants, lawyers, professionals (mining engineers and foresters) and management consultants will have easier access to practice in each country:

- Certification restrictions requiring registration in each country will be somewhat relaxed.

- The consulting industry will be pressured by an increased presence of consultants that don't have to maintain a local establishment.

- Access to skilled experts in certain fields such as educators from Alaska will allow an expansion of post secondary educational programs.

Tourism

Tourism service firms will be allowed easier cross-border flows of staff, equipment and supplies:

- There may be a reduction in the revenue that the Yukon earns from the industry if tourism facilities have more staff, supplies and equipment from the southern states.

- Tourism firms may bring in their own expert staff and supply their business from the U.S.

- Alaska has experienced the same problems as the Yukon from the presence of large southern tourism firms controlling the industry and gaining most of the benefits.

Construction and Contracting

Companies on both sides of the border have always had essentially free access to practice in each country. The main restriction was on labour mobility across borders:

- The agreement does ease provisions for temporary work entry for business purposes which will facilitate trans-border travel.

- Efforts to simplify standards and customs procedures will smooth the path for firms to practice in both countries.

- Construction firms will have more ability to win contracts in both countries. Local purchase and tendering practices will be restricted.

Cultural Industries

Cultural industries are excluded from the investment clause of the agreement. However, there is provision for the U.S. to claim that Canada is attempting to achieve an economic objective under the guise of culture. Given the U.S. definition of culture (which views publishing, media and movies as an entertainment industry), it is likely that they will have different views than Canadians.

Retail Services

Retailers will see two effects of the agreement on their business:

- Sourcing and importing of products from the U.S. will be easier and make their supply options broader. A more regionalized trade pattern may evolve within North America with Yukon firms obtaining supply from the U.S. west coast instead of more distant Canadian suppliers in Quebec and Ontario.

- Prices of products may be less as tariffs are reduced if transportation and warehousing do not consume these potential savings.

Financial Services

Canada has agreed to treat U.S. companies as Canadian nationals in the ability to purchase shares in Canadian financial institutions:

- This will provide greater penetration of the financial sector by the U.S. who can more heavily invest in Canadian banks, as well as having greater freedom to operate directly in Canada.

- Canada receives a "guaranteed" right of access to the U.S., something which at the present time is meaningless since many foreign banks operate in the U.S. It only has merit if threats to change U.S. bank legislation do go forward and exclude foreign banks.

- Given the size of the Yukon market, it is unlikely that U.S. banks will be attracted to establish here so there is little likelihood of benefit to the Yukon.

CONSUMERS

Estimating consumer gains from the trade Agreement is difficult. There are some studies that have shown annual gains of $20 or $800 per person depending on whose study method one chooses to accept. However, government may also see these gains as a potential source of tax revenue to make up for lost tariff revenue. A true test will also be the extent of consumer savings, if any, that businesses are prepared to pass on to the consumer.

CONCLUSIONS:

The Trade Agreement may retard Yukon efforts to achieve a key Yukon goal: to have greater control over our own future. In the short term, Canada has gained improved access to the U.S. market. In the long term, we may give up many important options.

A number of provisions within the agreement will alter the way the Government of the Yukon can promote development. We will have no ability to review investment decisions; the use of energy as an industrial incentive tool will be more limited; will be restricted against some local purchasing, tendering and procurement practices; and, have no guarantees that our development programs will not be disputed by the U.S.

Given the reality of the federal government commitment to push on with the trade initiative, we must look forward to see how we can adjust and adapt to the changes likely to come. All Yukoners must now look for ways to ensure that the Yukon can capitalize on the opportunities presented in the Agreement and minimize the dangers.

DEFINITIONS:

Tariffs:	A duty (or tax) levied upon goods transported from one region to another. Tariffs are used to increase the of imports which, in turn, assist domestic industries be competitive. As domestic industries have become more competitive, tariffs have been traditionally removed.
Non-Tariff Barriers:	Government measures or policies which affect the trade of goods and services. These include: local purchasing (procurement), local hire, regional development policies and, subsidies.